Instructor: Dr. Hall | **Accounting 460** | **Estimated time**

CPA Problems | **15-25 minutes**

Handout Problem No. F-97

This question consists of 6 items. Select the **best** answer for each item. Use a No. 2 pencil to blacken the appropriate ovals on the *Objective Answer Sheet* to indicate your answers. **Answer all items**. Your grade will be based on the total number of correct answers.

Hake Co. is in the process of preparing its financial statements for the year ended December 31, 1994.

Required:

Items 1 through 6 represent various transactions that occurred during 1994. The following **two** responses are required for each item:

- Compute the amount of gain, loss, or adjustment to be reported in Hake's 1994 financial statements. Disregard income taxes. To record your answer, blacken the ovals on the *Objective Answer Sheet*. If zeros precede your numerical answer, blacken the zeros in the ovals preceding your answer. **You cannot receive credit for your answers if you fail to blacken an oval in each column.** You may write the numbers in the boxes provided to facilitate blackening the ovals; however, the numbers written in the boxes will **not** be graded.
- Select from the list below the financial statement category in which the gain, loss, or adjustment should be presented, an blacken the corresponding oval on the *Objective Answer Sheet.* A category may be used once, more than once, or not at all.

Financial Statement Categories

A. Income from continuing operations.
B. Extraordinary item.
C. Cumulative effect of change in accounting principle.
D. Prior period adjustment to beginning retained earnings.
E. Separate component of stockholders' equity

1. On June 30, 1994, after paying the semi-annual interest due and recording amortization of bond discount, Hake redeemed its 15-year, 8% $1,000,000 par bonds at 102. The bonds, which had a carrying amount of $940,000 on January 1, 1994, had originally been issued to yield 10%. Hake uses the effective interest method of amortization, and had paid interest and recorded amortization on June 30. Compute the amount of gain or loss on redemption of the bonds and select the proper financial statement category.

2. As of January 1, 1994, Hake decided to change the method of computing depreciation on its sole piece of equipment from the sum-of-the-year's-digits method to the straight-line method. The equipment, acquired in January 1991 for $520,000, had an estimated life of five years and a salvage value of $20,000. Compute the amount of the accounting change and select the proper financial statement category.

3. In October 1994, Hake paid $375,000 to a former employee to settle a lawsuit out of court. The lawsuit had been filed in 1993, and at December 31, 1993, Hake had recorded a liability from lawsuit based on legal counsel's estimate that the loss from the lawsuit would be between $250,000 and $750,000. Compute the amount of gain or loss from settlement of the lawsuit and select the proper financial statement category.

4. In November 1994, Hake purchased two marketable equity securities, I and II, which it bought and held principally to sell in the near term, and in fact sold on February 28, 1995. Hake has adopted Statement of Financial Accounting Standards No. 115, *Accounting for Certain Investments in Debt and Equity Securities*. Relevant data is as follows:

		Fair Value	
	Cost	12/31/94	2/28/95
I	$125,000	$145,000	$155,000
II	235,000	205,000	230,000

   Compute the amount of holding gain or loss at December 31, 1994, and select the proper financial statement category.

5. During 1994, Hake received $1,000,000 from its insurance company to cover losses suffered during a hurricane. This was the first hurricane ever to strike in Hake's area. The hurricane destroyed a warehouse with a carrying amount of $470,000, containing equipment with a carrying amount of $250,000 and inventory with a carrying amount of $535,000 and a fair value of $600,000. Compute the amount of gain or loss from the hurricane and select the proper financial statement category.

6. At December 31, 1994, Hake prepared the following worksheet summarizing the translation of its wholly-owned foreign subsidiary's financial statements into dollars. Hake had purchased the foreign subsidiary for $324,000 on January 2, 1994. On that date, the carrying amounts of the subsidiary's assets and liabilities equaled their fair values.

	Foreign Currency amounts	*Applicable exchange rates*	*Dollars*
Net assets at January 2, 1994 (date of purchase)	720,000	$.45	$324,000
Net income, 1994	250,000	.42	105,000
Net assets at December 31, 1994	970,000		429,000
Net assets at December 31, 1994	970,000	.40	388,000

   Compute the amount of the foreign currency translation adjustment and select the proper financial statements category.